

**Testimony of Walter B. McCormick, Jr.
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Before the Senate Committee on Commerce, Science and
Transportation**

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Mr. Chairman, Co-Chairman Inouye and members of the Committee, I am Walter McCormick, president and chief executive officer of the United States Telecom Association (USTelecom).

At the outset, let me thank you for conducting this comprehensive series of hearings. USTelecom and its members have been honored to testify on net neutrality, universal service, video franchising, municipal networks, and rural issues. As this impressive fact-gathering process draws to a close, it is only fitting that you bring it all together with convergence and competition – two words that capture perfectly the environment in which telecom firms now operate.

For a century our organization was known as the United States Telephone Association. But the word “telephone” is becoming less and less descriptive of the business models and competitive strategies of our 1,200 member companies. Whether it’s AT&T or the Epic Touch Company in rural Kansas, companies are rapidly transforming. They are diversifying into high-speed Internet, wireless services, VOIP, and broadband television.

This is a significant change for these companies, some of which have been family-run telephone companies for a century or more. This diversification is the most far-reaching change in our industry today. It’s sweeping the country, almost without regard to population density or geography.

Our companies are racing to change the way they operate, and they need Congress to embrace change as well. We urge you to use two tools when you think about the future of our communications laws – a fresh perspective and a clean sheet of paper.

When the 1934 Communications Act was written, providing phone service was an expensive undertaking. Congress acknowledged the existence of a monopoly and created the FCC and a body of laws to ensure quality service and reasonable rates.

When the 1984 Cable Act was passed, Congress again accepted a monopoly arrangement and again established government as the one to protect consumers.

Today, there are a variety of networks, and the barriers to entry in voice, video, and broadband are relatively low for all but your local telecom service provider. For Internet access, consumers are using: DSL, cable modem, satellite, wireless, and electric power

lines. The range of video networks includes co-axial cable, satellites, wireless, and fiber-optic lines.

In fact, these days, it's not even necessary to build a network to compete in voice and video. Companies like Vonage, Skype, and Sun Rocket have millions of phone customers. A variety of new web sites allow anyone with an Internet connection to download movies, TV shows, or amateur video. Major sporting events are online now as well. In fact, you may recall the spate of media reports earlier this month regarding a possible drop in office productivity because employees could watch the NCAA basketball tournament on their computers.

Against this backdrop, the USTelecom board of directors met in November 2004 and unanimously adopted principles that we believe should serve as the foundation for updating our nation's telecom laws. These principles call for universal service reform and for a new regulatory approach, an approach geared to the creation of a competitive, consumer-driven market for communication services.

As I alluded to a few moments ago, a serious concern of USTelecom is legacy regulation that either prevents competition or creates a competitive disadvantage for those who invest in networks. For instance, the marketing materials of Sun Rocket, the Internet phone company, say subscribers can avoid universal service charges. And, online video providers are winning customers and gaining market share every day – with no thought of having to apply for a local franchise agreement.

Competition has already arrived in voice communication. But it is only emerging in video. The most significant communications policy challenge of the 109th Congress is how to hasten the development of full and fair competition in video.

If you are fortunate enough to be a cable television provider, you have effectively operated as a monopoly for 20 years, albeit with some competition from satellite. In the '96 Act, cable received authority to enter the telephone business – free from any legacy regulation, a position we did not oppose, since we believe consumers are better served — seeing more choice, innovation and lower prices — when companies are allowed to compete head-to-head in the marketplace. We hope that the cable industry will today urge the committee to take this same free market approach of lowering barriers to entry for new video entrants as local telecom service providers try to enter the video business.

Based upon its recent actions, we expect that cable will argue against our entry into video. Why compete in a free and fair marketplace when you have such a lucrative business arrangement as the cable companies currently do? Their pricing power has enabled them to raise rates 86 percent from 1995 to 2004. That's a figure generated by the FCC.

When USTelecom called attention to these increases the cable industry responded by refusing to run our factual ads in the DC area and many other places around the country. In an awkward attempt to try and justify these soaring prices, the cable industry insisted

that we take into account the rising number of channels. If you factor in additional channels, cable prices still have risen a whopping 57 percent from 1995 to 2004.

Whether you prefer to look at it as an 86 percent price increase or a 57 percent price increase, it's still a substantial number. And the cable companies fear new entry into video, because we are their most formidable competitor.

Time is money for consumers. Postponing franchise reform until the next session of Congress, that one year of delay, will cost consumers \$8 billion. A two-year delay would cost Americans nearly \$16 billion. This comes to about \$75 per household per year. This figure has also been broken down on a state-by-state basis, and the numbers are substantial. One year of delay in franchise reform would cost:

- Alaska consumers \$12 million;
- Hawaii consumers \$31 million; and
- Montana consumers \$22 million.

Consumers will pay a steep price for delay.

The GAO has studied trends in cable pricing and the effects of competition. It found that cable faces wireline competition in only 2 percent of its franchise areas. But wireline competition had an impact that satellite competition did not. The GAO found that prices were 15 percent lower where cable faced a wireline competitor.

Local franchising requirements impede our entry. They extend the period during which consumers will pay artificially high prices. Let me give you two examples:

- Ben Lomand Telephone Cooperative in McMinnville, Tennessee, has upgraded its network, and has the capacity to offer video service to approximately 60 percent of its 42,000 customers. However, in order to offer video, it must apply for and receive 25 different franchise agreements, some of which are required for areas in which it serves just 100-200 customers. After 18 months of trying, the company has received only 15 franchises.
- In the case of Verizon, one year after engaging in franchise negotiations with 95 local franchising authorities, only 10 have granted franchises and 85 remain in negotiation. Typically, the process takes 18 to 24 months.

Technology has created vigorous competition in voice and broadband. Unleashing the forces of competition and convergence in the video sphere will require a little help from Congress.

Consumers want a simpler life. They want one communications provider who can package their voice, video, and Internet into one bundle. And consumers want lower bills.

USTelecom members all across the country are hustling to give consumers what they want. We realize we cannot rely on old business models and old practices. The digital age has changed everything for our industry. Unfortunately, the benefits of this change

will be halted or delayed for millions of consumers unless Congress removes legacy regulations adopted in a different era and takes action to update our communication laws.

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